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DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 570

[Docket No. FR-5767-N-04]
RIN 2506-AC35

Section 108 Loan Guarantee Program:
Announcement of Fee to Cover Credit Subsidy Costs

AGENCY: Office of the Assistant Secretary for Community Planning and Development, HUD.

ACTION: Announcement of fee.

SUMMARY: This document announces the fee that HUD will collect from borrowers of loans guaranteed under the HUD's Section 108 Loan Guarantee Program (Section 108 Program) to offset the credit subsidy costs of the guaranteed loans pursuant to commitments awarded in FY 2016, as authorized by the Continuing Appropriations Act, 2016. Elsewhere in today's Federal Register, HUD is publishing a final rule that amends its regulations to permit HUD to collect fees for Section 108 guaranteed loans.

DATES: *Effective Date:* **[INSERT DATE THAT IS 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**.

FOR FURTHER INFORMATION CONTACT: Paul Webster, Director, Financial Management Division, Office of Block Grant Assistance, Office of Community Planning and Development, Department of Housing and Urban Development, 451 7th Street, SW, Room 7180, Washington, DC 20410; telephone number 202-708-1871 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the toll-free Federal Relay Service at 800-877-8339. FAX inquiries (but not comments) may be sent to Mr. Webster at 202-708-1798 (this is not a toll-free number).

SUPPLEMENTARY INFORMATION:

I. Background

Elsewhere in today's Federal Register, HUD is publishing a final rule that amends the Section 108 Program regulations to establish additional procedures when HUD is required or authorized to collect fees from Section 108 borrowers to offset the costs of the Section 108 loan guarantee commitments. Following consideration of the public comments submitted in response to HUD's February 5, 2015 (80 FR 6469) notice that proposed the fee required to offset the credit subsidy costs to the Federal government to guarantee Section 108 loans, HUD has determined to set the fee for Section 108 loan disbursements under loan guarantee commitments awarded in FY 2016 at 2.58 percent of the principal amount of the loan. As discussed below, and as HUD discusses in its final rule published elsewhere in today's Federal Register, HUD determined to not to impose a fee with respect to FY 2015 loan guarantee commitments. The public is directed to HUD's final rule for a detailed discussion by HUD of the significant issues raised by the public comments submitted in response to HUD's February 5, 2015, notice and HUD's response to those comments.

II. FY 2016 Fee: 2.58 Percent of the Principal Amount of the Loan

This document sets the fee for Section 108 loan disbursements under loan guarantee commitments awarded in FY 2016 at 2.58 percent of the principal amount of the loan. HUD will collect this fee from borrowers of loans guaranteed under the Section 108 Program to offset the credit subsidy costs of the guaranteed loans pursuant to commitments awarded in FY 2016, as authorized by the Continuing Appropriations Act, 2016 (Pub. L. 114-53, approved September 30, 2015). The calculation of the FY 2016 fee, which was specified in the FY 2016 President's

Budget¹, uses the same fee calculation model as the FY 2015 proposed fee included in HUD's February 5, 2015, notice, but incorporates updated information regarding the composition of the Section 108 portfolio and the timing of the estimated future cash flows for defaults and recoveries. The calculation of the fee is also affected by the discount rates required to be used by HUD when calculating the present value of the future cash flows as part of the Federal budget process.

As described in HUD's February 5, 2015, notice, HUD's credit subsidy calculation is based on the amount required to fully offset the credit subsidy cost to the Federal government associated with making a Section 108 loan guarantee. As a result, HUD's credit subsidy cost calculations incorporated assumptions based on: (i) data on default frequency for municipal debt where such debt is comparable to loans in the Section 108 loan portfolio; (ii) data on recovery rates on collateral security for comparable municipal debt; (iii) the expected composition of the Section 108 portfolio by end users of the guaranteed loan funds (e.g., third party borrowers and public entities); and (iv) other factors that HUD determines may be relevant to this calculation.

Taking these factors into consideration, HUD determined that the fee for disbursements made under loan guarantee commitments awarded in FY 2016 is 2.58 percent, which will be applied only at the time of loan disbursements. Note that future notices may provide for a combination of up-front and periodic fees for loan guarantee commitments awarded in future fiscal years but will be subject to the public comment provisions of § 570.712(b)(2) of the final rule.

¹ The FY 2016 President's Budget for HUD is available at: <https://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/hud.pdf>. The fee is specified in table 6 of the Federal Credit Supplement to the 2016 budget and is available at: https://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/cr_supp.pdf

As HUD discusses in response to public comment on the amount of the fee, the expected cost of a Section 108 loan guarantee is difficult to estimate using historical program data because there have been no defaults in the history of the program that required HUD to invoke its full faith and credit guarantee or use the credit subsidy reserved each year for future losses.² This is due to a variety of factors, including the availability of Community Development Block Grant (CDBG) funds as security. As authorized by Section 108 of the Housing and Community Development Act of 1974, as amended (42 U.S.C. 5308), borrowers may make payments on Section 108 loans using CDBG grant funds. Borrowers may also make Section 108 loan payments from other anticipated sources but continue to have CDBG funds available should they encounter shortfalls in the anticipated repayment source.

The fee of 2.58 percent of the principal amount of the loan will offset the expected cost to the government due to default, financing costs, and other relevant factors. To arrive at this measure, HUD analyzed data on comparable municipal debt over an extended 16 to 23 year period. The estimated rate is based on the default and recovery rates for general purpose municipal debt and industrial development bonds. The cumulative default rates on industrial development bonds (14.62 percent) were higher than the default rates on general purpose municipal debt (0.25 percent) during the period from which the data were taken. (The recovery rates for industrial development bonds and general purpose debt were 74.76 and 90.27 percent, respectively.) These two subsectors of municipal debt were chosen because their purposes and loan terms most closely resemble those of Section 108 guaranteed loans. In this regard, Section 108 guaranteed loans can be broken down into two categories: (1) loans that finance public infrastructure and activities to support subsidized housing (other than financing new

² U.S. Department of Housing and Urban Development, Study of HUD's Section 108 Loan Guarantee Program, (prepared by Econometrica, Inc. and The Urban Institute), September 2012.

construction) and (2) other development projects (e.g., retail, commercial, industrial). The 2.58 percent fee was derived by weighting the default and recovery data for general purpose municipal debt and the data for industrial development bonds according to the expected composition of the Section 108 portfolio by corresponding project type. Based on dollar amount of Section 108 loan guarantee commitments awarded during the period from FY 2010 through FY 2014, HUD expects that 25 percent of the Section 108 portfolio will be similar to general purpose municipal debt and 75 percent of the portfolio will be similar to industrial development bonds. In setting the fee at 2.58 percent of the principal amount of the guaranteed loan, HUD believes that the amount generated will fully offset the cost to the Federal government associated with making guarantee commitments awarded in FY 2016.

Dated: October 26, 2015

Harriet Tregoning, Principal Deputy Assistant
Secretary for Community Planning and
Development

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